



## **Cottage Sites**

An Overview | Updated March 20, 2013

### **Background**

Idaho was granted millions of acres of land at statehood by the federal government. The terms and conditions of the land grants were very specific - to generate money and provide long-term financial support to the new state's public school system and other institutions.

The land is referred to as state endowment trust land and the authority to make decisions on the management of these lands is given to the State Board of Land Commissioners (Land Board) in Idaho's Constitution. The Constitution mandates that the lands produce "maximum long-term financial returns" to the trust beneficiaries.

Some of the land granted to Idaho included the land surrounding parts of Priest Lake and Payette Lake. Since the early 1900s the State has been leasing the land as residential sites, known as cottage sites. The individuals and families who leased the lots over time built homes on them, creating a split estate where the structure or "improvement" is considered personal property owned by the private individual (lessee) and the State owns the land underneath, including all of the associated rights of a surface owner.

### **A New Era for Cottage Sites**

For the past several decades some cottage site lessees have expressed a desire to purchase the lot underneath their home.

A series of public auctions occurred in the late 1970s and early 1980s related to the disposition of cottage properties. In the late 1990s land exchanges involving cottage site properties were completed, and most recently two cottage sites were disposed of at public auction at Payette Lake in 2011. The outcome of the land exchanges was the acquisition of a variety of asset types, including commercial buildings and parking lots in downtown Boise, and timberland tracts.

Given the personal nature of the cottage sites and the foreseeable difficulty in obtaining market rent into the future, the Land Board and the Idaho Department of Lands (IDL) concluded that it was in the best interest of the endowment trusts to develop a plan to divest the State's interest in most of the lots over time and reinvest in other assets that could produce higher returns for the endowment trusts.

The Land Board voted in February 2010 to direct the IDL to develop a plan that would unify ownership by transitioning the lots into private ownership through auction or exchange, or the State acquiring the lessee improvements to bring the lot and the structure on it under ownership of the State. The goal is to reposition the State's trust land portfolio over a period of time.

### **Cottage Site Plan**

With the help of real estate consultants, legal counsel specializing in real estate and land use law, and in-house planners, the IDL developed the Cottage Site Plan for Land Board consideration.

The primary objective of the Cottage Site Plan was to articulate a programmatic "market savvy" process for unifying the split cottage site estates. The processes to be employed should be the same processes that a prudent institutional real estate investor would use when seeking to maximize the long-term financial return to beneficiaries or shareholders. The plan reiterated the need for the Land Board to authorize flexibility in offering transactions that are consistent with modern real estate practices and at the same time keep with the transaction requirements specified by the Constitution, such as land exchange or public auctions for land sales.

The IDL gathered public input on the plan, which eventually was adopted by the Land Board in 2010, along with the necessary “Lot Solutions Process.”

## Lot Solutions Process

The Lot Solutions Process was needed in order to prepare the lots to be ready for sale or exchange in a twenty-first century real estate market. Over a period of several decades the cottage site leases had been offered to potential lessees in an “as is” condition, raw land and nothing more. Access roads, dry utilities (electrical power, cable, telephone), wet utilities (sewer and water) and the roles and responsibilities for the use and care of common areas, like roadways and access ways to the lake front, had not been developed or documented.

The IDL stakeholder outreach during the Lot Solutions Process provided an opportunity for lessees to provide input into the platting process. A total of 10 neighborhood meetings were held for lessees at both Priest and Payette Lakes, giving all parties the opportunity to have their questions answered in person by IDL staff. The IDL also provided consistent points of contact and utilized multiple methods of communication in providing updates, including e-mail, direct mail, Web sites, and lessee association assistance in distributing important information. A total of 682 draft plat packets also were mailed to lessees and deeded cottage site owners in 2012.

Recordation of the new plats began in January 2013, making the cottage sites eligible for transactions. As of March 20, 2013, all plats at Priest Lake have been recorded and the platting at Payette Lake is expected to be completed by summer 2013 because of a more complex ownership pattern around Payette Lake.

## Cottage Site Land Sales (via public auction)

The Constitution requires a **public auction** for the disposal of state endowment trust land.

The auction process for cottage sites is voluntary and is initiated by the current lessee, not IDL or a third party. The IDL anticipates conducting a voluntary auction cycle annually, subject to market conditions and Land Board approval.

When the current lessee submits an application for cottage site land sale, they would be required to pay a \$500 nonrefundable application fee. After the lot and the lessee-owned improvements are appraised, the applicant may choose to proceed with an auction or cancel the application and continue leasing. If the applicant chooses to proceed with the auction, a one percent auction administration fee is charged, to be refunded if the applicant is not the successful bidder.

A successful bidder other than the current lessee would be required to pay a nonrefundable deposit that includes the appraised value of the improvements, an appraisal fee, and the one percent auction administration fee. If the lessee is not the successful bidder then they would receive the value of the improvements on or before the close of escrow.

Land sales in particular impact local real estate prices. It would not be in the best interest of the endowment trust beneficiaries or the local community to make more cottage sites available for auction than the market will bear, so the timing of the auction cycles and the number of sites offered will be determined by the IDL, using market conditions as a guide. Recreation properties such as the cottage sites typically sell during the summer and early fall seasons.

Given the fact that there are more than 500 cottage sites at both Priest and Payette Lakes, it may be some time before the State completely divests its interest in all of the cottage sites. Another option, one that does not impact the real estate market, is the land exchange.

## Land Exchange

At any time, the owner of investment property(ies) may propose an equal value exchange of investment property(ies) that meet the IDL underwriting requirements for cottage site lots. Upon acquisition of the cottage site lots, the new owner or its licensed broker can negotiate with a lessee or group of lessees to lease or sell the cottage site lots

through any means available in the open market. Participation in the land exchange process is voluntary for lessees. Pre-application meetings are required and the Land Board and IDL will base its consideration of the proposal on whether it is in the long-term best interest of the endowment trust.

Several information pieces have been written to explain how IDL will manage cottage site land exchanges or voluntary land sale auctions, and the related fees. The information can be found on the IDL Web site at this link: <http://www.idl.idaho.gov/am/cottage-site-transactions.html>

## Wasden v. Land Board

The Idaho Constitution states that disposal of state endowment trust land must occur through a public auction if two or more parties apply to lease the same land. Disposal has been determined through Constitutional debate discussions and case law to **include both direct sales and leasing** of state endowment trust land.

The Legislature in 1990 passed a law that excluded cottage sites leases from the public auction requirement, limiting competitive opportunities for other parties to bid on the lease and thus limiting the potential to generate higher returns for the endowment trusts.

Attorney General Lawrence Wasden challenged that law and the Idaho Supreme Court in July 2012 decided the law was indeed unconstitutional, subjecting the cottage site leases again to the public auction requirement when two or more applicants are interested in leasing the same site.

All 534 cottage site leases set to expire on December 31, 2013, will be made available for anyone to lease.

The decision also served to assert the Board's authority in matters related to management of state endowment trust lands.

## What can lessees expect with cottage site leasing in the near future and the long term?

There has been some confusion about the auction process for cottage site land sales, which was outlined on page 2, and the auction process for cottage site leasing, which is outlined below.

As a result of the *Wasden* case, cottage site leases are subject to the public auction requirement. If more than one applicant (i.e. the current lessee and another person), desires to lease the same site then the lease is subject to the public auction requirement, similar to all other types of endowment leases.

The existing two-year cottage site leases at Priest Lake and Payette Lake will expire on December 31, 2013. In anticipation of this expiration date and based on the Idaho Supreme Court opinion, the IDL will take the following steps in the issuance of new cottage site leases.

### 1. Development of the 2014 Rent Amount

Under the new Idaho Supreme Court opinion, I.C. § 58-310(5) now applies to cottage site lease applications and will require that **challengers of current cottage site leases pay to the IDL one year's rent at the time of application.**

Idaho Code establishes that the deadline for application for expiring leases is on April 30 of the year of expiration, in this case April 30, 2013.

In March 2013, the IDL established the 2014 rent amount for each cottage site lease in order to properly communicate the requirements of a complete application to potential challengers of a cottage site lease prior to the deadline.

### 2. Development and Implementation of Staggered Leases

Because the current cottage site leases all expire on December 31, 2013, the IDL will make available to the open market the entire group of more than 500 cottage site leases at the same time.

In order to spread out the future availability of cottage site leases to maximize opportunities for competition, the IDL will offer 2014 cottage leases with staggered lease lengths ranging from five to ten years, so that approximately 16% of the future leases expire in any given year.

Under this approach, the IDL will create cottage site lease groups broken out by lake, by geographic location at each lake, and by waterfront/non-waterfront class (at Payette Lake), establishing approximately six groups at each lake. The IDL will randomly assign lease lengths of five to ten years to each cottage site lease within each group.

In order to appropriately communicate the 2014 cottage site lease application process to existing lessees the IDL mailed this information to each cottage site lessee on March 25, 2013. The information will also be posted on the IDL Web site to communicate the process to all prospective applicants.

### **3. Advertisement of Expiring Leases**

The IDL will post the list of expiring cottage site leases to the Department's Web site along with information about application deadline, 2014 rent amounts due by challengers of the lease, lease locations and lease lengths. In addition, the IDL will place ads in preferred media outlets to best communicate the general availability of cottage sites for lease.

### **4. Providing Applications and Lease Templates**

The IDL will provide copies of the Application for Use Form and cottage site lease template to each existing cottage site lessee and upon request to any potential challenger of an existing cottage site lease.

Any challenger will be required to provide the following by the April 30, 2013 application deadline:

- submission of a completed Application for Use Form
- payment of the \$250 nonrefundable application fee
- and payment of the 2014 rent amount

Existing lessees will only be required to provide the completed Application for Use Form and the \$250 application fee by the application deadline. The cover letter to existing lessees will identify the length of the lease being offered and the 2014 rent amount.

### **5. Implementation of the Conflict Auction Process**

If more than one complete application is received for a cottage site lease, the IDL will notify each applicant of the lease conflict.

The IDL then will proceed with the valuation of any approved improvements (personal property) on the site using a contracted appraiser.

Notices will be sent to the applicants of the pending auction according to Idaho Code, which requires the IDL to provide a 14-day written notice of the time and place of the auction.

Prior to commencement of the auction, challengers of an existing cottage site lease will be required to deposit with the IDL an amount equal to the appraised value of the lessee's approved improvements (personal property).

At the next regularly scheduled board meeting following the auction, the IDL will present the auction results to the Land Board for final approval. Idaho Code allows the Land Board to reject any and all bids made at an auction, when in their judgment there has been fraud or collusion, or for any other reason, which in the judgment of the Land Board justifies the rejection of said bids.

If the existing lessee is not awarded the lease, the IDL will disburse payment for the approved improvements to the existing lessee from the deposit of the successful challenger. Any challenger who is not awarded the lease will receive a refund of their first year's rental deposit and improvement deposit.

**In the long term**, again given the fact that there are more than 500 cottage sites at both Priest and Payette Lakes, it may be some time before the State completely divests its interest in all of the cottage sites. Current cottage site lessees should expect to continue participating in the cottage site leasing program in the years ahead.